88-489

No._____

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

October Term, 1987

Dwight A. McKabney and Mercedes P. McKabney
Petitioners,

v.

United States of America,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

Dwight A. McKabney
Mercedes P. McKabney
P.O. Box 1538
APO Miami, Fl. 34003
Telephone (011) 507-63-5316
Republic of Panama
Petitioners, Pro Se

September 19, 1988

550 pw

QUESTIONS PRESENTED

This Court decided, in *O'Connor v. United States,* 479 U.S. 27, 107 S.Ct. 347 (1986), that a provision of the 1977 Panama Canal Treaty was not intended to create an exemption from federal income tax for American citizen employees of the canal agency. The Court's opinion relied on certain acts and omissions attributed to government officials of Panama as being indicative of the treaty's intended meaning.

The questions presented are:

1. Was it a denial of constitutional due process for the claims court to refuse to grant these petitioners an evidentiary hearing and the opportunity to show that extrinsic fraud pervaded the U.S. Government's defense in *O'Connor?*

2. If the treaty interpretation by this Court in 1986 is shown to have been based upon false or inchoate evidence adduced by the government, is the lower court required to adhere to that original decision?

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED. i
OPINIONS BELOW 1
JURISDICTION. 2
TREATY AND STATURORY PROVISIONS INVOLVED. 3
STATEMENT OF THE CASE 5
REASON FOR GRANTING THE WRIT 10

THE FEDERAL CIRCUIT'S DECISION TO AFFIRM THE DENIAL OF AN EVIDENTIARY HEARING COUNTENANCES THE PERPETRATION OF EXTRINSIC FRAUD BY THE FEDERAL GOVERNMENT IN LITIGATION TO WHICH IT IS A PARTY 10

CONCLUSION 19

APPENDIX

A. DECISION OF U.S. COURT OF APPEALS, FED. CIR. JUNE 20, 1988, IN *MCKABNEY V. U.S.* 1a

B. ORDER OF U.S. CLAIMS COURT, DEC. 3, 1987, IN *MCKABNEY V. U.S.* 3a

C. JUDGMENT OF U.S. CLAIMS COURT, DEC. 4, 1987, IN *MCKABNEY V. U.S.* 4a

D. OPINION OF U.S. CLAIMS COURT, AUG. 13, 1987, IN BONANNO V. U.S. 5a

E. JUDGMENT, U.S. COURT OF APPEALS FOR FED. CIR., JUNE 20, 1988, IN MCKABNEY V. U.S. . . . 14a

F. DRAFT OF ARTICLE XVI OF AGREEMENT IN IMPLEMENTATION OF ARTICLE IV OF PANAMA CANAL TREATY OF 1977, FEB. 4, 1975 ..... 15a

G. EXCERPT FROM TRANSCRIPT OF PROCEEDINGS OF BOARD OF DIRECTORS' MEETING, PANAMA CANAL COMMISSION, JULY 1984..... 18a

H. AFFIDAVIT OF DR. ARISTIDES ROYO, TREATY NEGOTIATOR AND EX-PRESIDENT OF PANAMA, OCT. 2, 1986 ..... 25a

I. ORDER OF U.S. CLAIMS COURT, FEB. 3, 1988, IN BONANNO V. U.S. (DENIAL OF MOTION TO VACATE JUDGMENTS, BUT WITH RIGHT TO REOPEN FOLLOWING APPEAL IN *MCKABNEY* V. *U.S.*) 30a

TABLE OF AUTHORITIES

CASES: PAGE

Bonanno v. *United States*, 12CL.CT. 769 (1987).... 2,6

Coplin v. *United States*, 6 CL.CT. 115(1984)..... 11,16,18

Coplin v. *United States*, 761 F.2D, 688 (FED.CIR.1985)..... 6,13,14

Corliss v. *United States*, 567 F. SUPP 162 (W.D. ARK. 1983)..... 5

Harris v. *United States*, 585 F.SUPP. 862 (S.D. GA. 1984)..... 5

Harris v. *United States*, 768 F.2D 1240 (11TH CIR. 1985)..... 6

Highley v. *United States*, 574 F.SUPP. 715 (M.D. TENN. 1983)..... 5

O'Connor v. *United States*, 479 U.S. 27, 107 S.CT. 347 (1986)..... *passim*

Salvation Army v. *Morris*, 421 F.2D 805, 807 (10TH CIR. 1970)..... 19

Sumitomo Shoji America, Inc. v. *Avagliano*, 457 U.S. 176 (1982)..... 16

Swearingen v. *United States*, 565 F.SUPP. 1019 (D. COLO. 1983)..... 5

United States v. *Reynes*, 50 U.S. (9 HOW) 127, 147-48 (1850)..... 16,18

TREATY DOCUMENTS:

AGREEMENT IN IMPLEMENTATION OF ARTICLE III OF THE PANAMA CANAL TREATY, SEPT. 7, 1977, UNITED STATES-PANAMA, T.I.A.S. Nº10031, ARTICLE XV(2)..... *passim*

Table of Authorities Continued

	Page
Agreement in Implementation of Article IV of the Panama Canal treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. №10032, Article XVI(2)	*passim*
Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. №10030, Article III.	3,16
Statutes:	
United States Code, Title 26, sec. 894(a)	4
Pub. L. № 96-70, 93 Stat. 456	5
Miscellaneous:	
J.N. POMEROY, Equitable Remedies, 2: 649 (1905)	18

IN THE

Supreme Court of the United States

October Term, 1987

Dwight A. McKabney and Mercedes P. McKabney,
Petitioners,

v.

United States of America,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

The petitioners Dwight A. McKabney and Mercedes P. McKabney respectfully pray that a writ of certiorari be issued to review the judgment and opinion of the United States Court of Appeals for the Federal Circuit, entered in the above-entitled proceeding on June 20, 1988.

OPINIONS BELOW

The opinion of the Court of Appeals for the Federal Circuit is not to be reported. It is reprinted in the appendix hereto, p. 1a, *infra.*

The order and judgment of dismissal by the United States Claims Court have not been reported. They are reprinted in the appendix hereto, pp. 3a and 4a, *infra*. The opinion cited by the Claims Court as the basis for dismissal of petitioners' suit is *Bonnano et ux. v. United States,* which is reported at 12 Cl.Ct.769 (1987), and is reprinted in the appendix hereto, p. 5a, *infra*.

JURISDICTION

Invoking federal jurisdiction under 28 U.S.C. sec. 1491, petitioners brought this suit in the Claims Court on January 15, 1986. That court, on December 4, 1987, dismissed the action without trial. See p. 4a, *infra*.

On petitioners' appeal, the Federal Circuit entered a judgment and opinion on June 20, 1988, affirming the Claims Court's order. See p. 1a, infra. No petition for rehearing was sought.

The jurisdiction of this Court to review the judgment of the Federal Circuit is invoked under 28 U.S.C. sec. 1254(1).

TREATY AND STATUTORY PROVISIONS INVOLVED

Panama Canal Treaty between the United States of America and Panama, September 7, 1977, T.I.A.S. No. 10030:

ARTICLE III
Canal Operation and Management

* * * * *

9. The use of the areas, waters and installations with respect to which the United States of America is granted rights pursuant to this Article, and the rights and legal status of the United States Government agencies and employees operating in the Republic of Panama pursuant to this Article, shall be governed by the Agreement in the Implementation of this Article, signed this date.

* * * * *

Agreement between the United States of America and Panama in Implementation of Article III of the Panama Canal Treaty September 7, 1977, T.I.A.S. No. 10031:

ARTICLE XV
Taxation

* * * * *

2. United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they

shall be exempt from payment of taxes, fees, or other charges on income derived from sources outside the Republic of Panama.

* * * * *

Agreement between the United States of America and Panama in Implementation of Article IV of the Panama Canal Treaty, September 7, 1977, T.I.A.S. No. 10032:

ARTICLE XVI
Taxation

* * * * *

(2) Members of the Forces or the civilian component, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United States Forces or for any of the service facilities referred to in Article XI or XVIII of this Agreement. Similarly, as is provided by Panamanian law, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

* * * * *

26 U.S.C. sec. 894(a):

(a) Income exempt under treaty. Income of any kind, to the extent required by any treaty

obligation of the United States, shall not be included in gross income and shall be exempt from taxation under this subtitle.

STATEMENT OF THE CASE

Petitioners brought suit in January 1986 in the U.S. Claims Court to recover federal income tax paid on salary earned in the Republic of Panama. The basis for the claim was a provision of treaty law that, by its plain terms, exempts such salary from "any taxes, fees, or other charges." This is Article XV(2) of the Agreement in Implementation of Article III of the Panama Canal Treaty, *supra.*

The compensation was paid during the years 1979 to 1981 by the Panama Canal Commission, an agency created pursuant to the 1977 treaty between the Republic of Panama and the United States. (Although "chartered" under an Act of Congress, Pub.L. No. 96-70, 93 Stat.456, Sept. 27, 1979, the Commission is required to be operated by a supervisory board composed of five Americans and four Panamanians, named by their respective governments.)

At the time petitioners sued, there were several hundred similar cases pending in the federal courts or that had been decided in the trial courts. 1/ In at least four instances, the litigation had progressed beyond the appellate level, and petitions for certiorari had been, or

---

1/ E.g. *Swearingen v. United States*, 565 F.Supp. 4019 (D. Colo. 1983); *Corliss v. United States*, 567 F.Supp. 162 (W.D. Ark. 1983); *Highley v. United States*, 574 F.Supp. 715 (M.D. Tenn. 1983); and *Harris v. United States*, 585 F.Supp. 862 (S.D. Ga. 1984).

later were to be, granted by this Court. 2/

Petitioners' suit, together with numerous others, was suspended without action in the claims court awaiting review by this Court of the *Coplin, O'Connor* and *Mattox* cases. The decision, adverse to the taxpayers, was handed down November 4, 1986, in *O'Connor v. United States*, 479 U.S. 27, 107 S.Ct. 347.

Subsequently, most of the suits in the claims court were dismissed; however, approximately 50 (including the petitioners') remained on the docket pending an effort by counsel to obtain a trial at which evidence could be introduced bearing on the intent of the parties to the Panama Canal treaty. (The *Coplin--O'Connor* litigation purportedly had been disposed of on summary judgment motions .)

The claims court in August 1987 denied a motion for further proceedings in *Bonnano v. United States*, 12 Cl.Ct. 769 (1987), and dismissed that suit. See p. 5a, *infra*. The present petitioners' action was also dismissed, without trial, on the ground that it involved the same issues as *Bonanno*. See order and judgment at pp . 3a and 4a , *infra*.

2/ *Coplin v. United States*, 761 F.2d 688 (Fed.Cir. 1985); *O'Connor v. United States* and *Mattox v. United States* (both cases were consolidated with *Coplin); Harris v. United States*, 768 F.2d 1240 (11th Cir. 1985).

The McKabneys noticed an appeal to the Federal Circuit. Counsel for the Bonannos moved to vacate the dismissal in their case as well as in the others. The claims court denied the motion without prejudice -- stating that the court will entertain motions to reopen "following the outcome of the appeal in *McKabney et al.*" See App. I, p. 30a, *infra.*

The McKabney appeal rested on the apparent irregularities that had been noted in the Government's handling of numerous cases in various judicial districts -- all of which cases asserted the claim of tax exemption under Article XV(2) of the treaty agreement. Although disposition of the three test cases on summary judgment should have meant that there were no material issues of fact, petitioners saw that Justice Scalia's decision in *O'Connor* had turned on (or was materially supported by) assumptions that, demonstrably, are in error. Those misconceptions, the appeal contended, were due to acts or omissions on the part of the executive branch that constituted extrinsic fraud and had deprived the O'Connors of the means of fully exhibiting their case.

The McKabneys' brief in the appellate court noted that this Court's decision in *O'Connor* had been based not only on the text of the treaty agreement, but also (in keeping with long-established practice) had drawn on factual material which it thought to be true. The supposed circumstances upon which the Scalia opinion relied were: --

(a) The determination by the United States (that it would not grant the tax exemption) had "gone unchallenged by Panama."

(b) The four Panamanian members of the board of directors of the Panama Canal Commission "did not object" to the construction that the U.S. had placed on Article XV(2).

(c) The text of Articles XV(2) and XVI(2) resulted from "the American side's own internal drafting" and, therefore, the final form had not been changed at Panama's request or with that government's approval.

(d) The full history or record of the negotiations on the subject had been revealed and contained "only a single (unhelpful) reference to United States' income taxation."

In their appeal below, the McKabneys contended that these four statements were untrue and should be tested through discovery and trial.

The Government argued that because "treaty interpretation is a question of law, not of fact, there is no reason to allow taxpayers an evidentiary hearing." With respect to the matter of the accuracy of the information upon which Justice Scalia relied, the Government's brief says: --

> ". . .the taxpayers' allegedly 'new' evidence was either presented to the Supreme Court for its consideration in the *O'Connor* case or is insufficient to warrant further reconsideration of the Supreme Court's interpretation of Article XV(2)."

In the light of what petitioners believed were the Government's aberrancies, it was urged upon the appellate court that the *O'Connor* decision should not be treated as having fixed the meaning of Article XV(2) like a fly in amber. The McKabneys contended that under those circumstances, the refusal of the claims court to grant them and the remaining claimants an evidentiary hearing was a deprivation of constitutional due process.

The Federal Circuit, however, recited the same conclusion as the claims court -- deciding that petitioners' action is foreclosed by the decision of this Court in *O'Connor*. See App. A, p. 1a, *infra*. It is that ruling which the present petition addresses.

REASON FOR GRANTING THE WRIT

THE FEDERAL CIRCUIT'S DECISION TO AFFIRM THE DENIAL OF AN EVIDENTIARY HEARING COUNTENANCES THE PERPETRATION OF EXTRINSIC FRAUD BY THE FEDERAL GOVERNMENT IN LITIGATION TO WHICH IT IS A PARTY

This petition is based upon a provision of the bilateral treaty agreements between Panama and the United States regarding the Panama Canal. The McKabneys' case is at the trailing edge of the group of several hundred lawsuits which from about 1981 to 1986 were filed in numerous federal courts in at least five judicial circuits. All of those plaintiffs sought to challenge the denial by the Internal Revenue Service of the income tax exemption that appears in plain language in the 1977 Panama Canal Treaty.

The McKabneys concede that this Court, in *O'Connor v. United States,* 479 U.S. 27, 107 S.Ct. 347 (1986) construed the provision in question (Article XV(2)) adversely to their claim. Nevertheless, they assert the right to an evidentiary hearing in their own case in the trial court for the following reasons:

(a) The *O'Connor* litigation was decided without trial, i.e., nominally on summary judgment. The actual situation was, however, that the

Federal Circuit and this Court thereafter relied upon certain facts as to which material issue was joined, but never resolved.

(b) In deciding *O'Connor,* neither the Federal Circuit nor this Court utilized the special procedure that may be invoked by the court in matters of treaty or international agreement to determine intent of the parties. Had this been done, the government would have been instructed to produce relevant diplomatic statements and correspondence, which even yet are undisclosed.

(c) By concealing pertinent evidence and by deliberate misrepresentation, the government established a false picture of how the treaty provision, Article XV(2), was negotiated and later interpreted by the Government of Panama. This Court's reliance on those distorted data led (as hereinafter shown) to conclusions that, petitioners urge, are visibly erroneous.

(d) The teaching of *O'Connor* is inapplicable to the facts that would be adducible in a trial of the McKabney claim.

In the claims court in *Coplin,* the government filed an affidavit by an official of the State Department (one John W. Stahlman) purporting to show that all of the contemporaneous negotiating records pertaining to what became Article XV had been produced pursuant

to the discovery requests of the plaintiffs. At trial, the McKabneys would challenge the veracity of the Stahlman report. The basis for such a challenge is not unsubstantial. See App. F, p. 15a, *infra.*

In, *O'Connor,* Justice Scalia made specific reference to the fact that the plaintiffs there could point to no Panamanian negotiating proposal supporting what he called the speculation that Panama would not accept a unilateral tax-exemption provision but would accept a bilateral one. He characterized the idea as "not inordinately credible on its face." *O'Connor*, slip opinion at 8, 107 S.Ct. at 352. The reason that the O'Connors had no document that would have given credence to their theory was that the State Department had embosomed such evidence, despite the legitimate requests for disclosure.

The relevant document that should have been produced was the *draft of Article XVI* of the Agreement in Implementation of Article IV of the Canal treaty, which on February 4, 1975, had been agreed to by the negotiators for the United States and the Republic of Panama. The relevant portion of that document reads as follows:

> "(2) Members of the forces or the civilian component, and dependents, shall be exempt from taxes, assessments, or other charges *to the Republic of Panama or any entity or political subdivision thereof* on income received as a result of

their services with or, employment by the United States Government. . . . " (Emphasis added.)

The foregoing provision must then be compared with the text of Article XVI(2) as it finally appeared in the treaty agreement in 1977. In pertinent part, that final version reads as follows:

"(2) Members of the Forces or the civilian component, and dependents, *shall be exempt from any taxes, fees, other charges on income received* as result of their work for the United States Forces." (Emphasis added.) (T.I.A.S. 10032, Sept. 7, 1977.)

There can be no dispute as to the difference in the "plain meaning" between the unilateral exemption (from Panama taxes) in the 1975 version -- agreed to by both countries -- and the bilateral exemption that in 1977 was incorporated in the finished treaty package. Why the change occurred and at the instance of which country are matters to be revealed in the trial court process, but the fact of the revision itself provides this Court with ample grounds for remanding the cause since it (more than merely tentatively) answers the question raised by Justice Scalia.

The reason that the nonproduction of this documen by the government for use of the *Coplin-O'Connor* plaintiffs was material (and in the light of the Stahlman affidavit, inexcusable) is that the

government's position throughout the course of the *O'Connor* litigation was that Article XV(2), governing taxation of Canal Commission employees had been adopted from and patterned after Article XVI(2), which dealt with taxation of the members and civilian employees of the United States military component.

As the "unproduced" document reveals, the military provision was agreed to more than two years before the negotiation of Article XV(2) took place in 1977. It will be incumbent upon the government to disclose the rationale, thus far shrouded in secrecy, that caused the parties to change their 1975 agreement with its explicit exemption from Panamanian taxes alone to the final 1977 version that speaks of exemption from *any taxes* and omits *"to the Republic of Panama or any entity or political subdivision thereof"*.

The due-process issue also arises out of other aspects of the government's conduct throughout the course of this multijurisdictional litigation, which in *Coplin* extended over a period of more than five years. The defendant's policy of obfuscation culminated in the Federal Circuit in March 1985 at the *Coplin* hearing when the government produced, on the morning of oral argument, a diplomatic note that was said to have just come to the State Department from the Government of Panama.

As the case moved on to oral argument in this

Court in October 1986 , the mystery of the message from Panama deepened when government counsel twice told this Court that the United States had *not solicited* the diplomatic note. Given the fact that the treaty had been signed nine years earlier, it is not surprising that Justice Scalia was moved to ask rhetorically whether Panama had suddenly just slipped the note under the door.

There is a marked inconsistency between counsel's statement to the Court and the affidavit of one of the principal Panamanian negotiators, former President Aristides Royo, which asserts that his interpretation was solicited in early 1985 by an attorney from the Department of State. See App. H, p. 27a, *infra*. Upon trial, the McKabneys would seek to resolve this conflict through discovery of official documents or by deposition of the personnel involved.

It was appropriate that the Court should give weight, in *O'Connor* to what it believed to be the position of the Panamanian government; howerer, Justice Scalia rejected the diplomatic note of February 1985 as a source of such information regarding Panama's view. (See slip opinion, p. 6, n. 2; 107 S.Ct. at 351.) The Justice did conclude, however, that neither Panama nor its four nationals on the Panama Canal Commission's board of directors had objected to the fact that the United States proceeded to collect income taxes from its U.S. citizen employees.

In this connection, the Court's attention is

invited to a transcript of the remarks made in July 1984 by two of the Panamanian board members. See App. G, p. 18a, *infra*. Those officials stated very clearly not only that the treaty agreement provides an exemption from U.S. income tax, but also that the American negotiators planned it that way. As board members named by Panama, they were participating officially and speaking on behalf of their government in the management of the Panama Canal as contemplated by Article III of the treaty.

Their statements regarding the interpretation of Article XV(2) plainly fall within the rule of *United State v. Reynes*, 50 U.S. (9 How.) 127, 147-48 (1850) and its progeny, e.g. *Sumitomo Shoji America, Inc. v. Avagliano*, 457 U.S. 183-184 (1982). The transcript was not produced by the government and, thus, was not introduced in *Coplin*. It *would* become part of the record in a trial of the McKabney claims.

The disordered and incomplete state of the record in *O'Connor* may also have contributed to another of the demonstrable errors in the opinion. Justice Scalia wrote:

> "A person receiving a Commission salary for work performed in, for example, Bogota would seem plainly to qualify for exemption under this provision -- rendering the second sentence, on the petitioner's understanding superfluous."

That conclusion is incorrect. The Court overlooked the

fact that Article I of the treaty agreement being interpreted specifically limits the application of the disputed Article XV(2) to United States citizen employees of the Commission who are *assigned for duty in the Republic Panama.* Agreement in Implementation of Article III of the Panama Canal Treaty, TIAS 10031, Sept. 7, 1977. The source of salary from outside Panama for Commission work in the Republic of Panama can be shown to be Washington, D.C. It is from there that a *portion of their compensation* is paid to those re-employed annuitants who return to federal service with the Commission in Panama.

With respect to the matter of whether Panama (other than via its four Commission board members) disagreed with the I.R.S. position on the income tax in question, the trial court would have to consider, and sift through, the uncertain but clearly contradictory evidence. For example, Dr. Cardoze, speaking for the Panama Government in July 1984 told the American officials to go to the U.S. Treasury and give the income tax back to the Commission employees. (App. G, p. 23a). The same Dr. Cardoze only seven months later took the opposite view when he issued the diplomatic note that magically appeared in the Department of State and was introduced by the government in the Federal Circuit on the eve of oral argument in the *Coplin-O'Connor* appeals.

It can reasonably be argued, at such a trial, that the views of the actual negotiators of Article XV(2)-- such as ex-President Royo (App. H, pp. 25a-27a) -- are more within the contemplation of *United States* v. *Reynes,* 50 U.S. (9 How.) 27, 47-48 (1850) than is the institutional declaration of a foreign government the recognition of which is presently suspended.

Whatever one might conclude, at this stage, regarding

the probable intention of the two countries in revising the original treaty language (from a regular Status of Forces tax exemption) to read as Articles XV(2) and XVI(2) now do, there can be no argument about the proposition that the government has dishonestly constricted the record in this litigation. (E.g., the successful use by the Justice Department in numerous cases of the Kozak affidavit -- later admitted to be spurious for the purpose that it was offered. *Coplin* v. *United States*, 6 Cl.Ct. at 132, n. 16).

It is the McKabneys' position that they have been denied due process of law in their effort to try the isssue of entitlement to refund of taxes they have paid on Commission salary for the years in question. The denial of an evidentiary hearing prevented them from fully exhibiting their case. They are entitled to have the judgment of dismissal set aside and to be granted an opportunity to present evidence. 2 J.N. POMEROY, Equitable Remedies 649 (1905). The extrinsic fraud of the government lay in its concealing material or controlling facts, despite a legal duty to disclose, for the purpose of taking undue advantage of the opposite parties. Not only did the executive branch conceal such evidence, but it also perfunctorily rejected the offers by the trial court (*Coplin,* 6 Cl.Ct. at 147) of additional time to come forward with relevant data.

Equitable relief from a judgment may be obtained on the ground of extrinsic or collateral fraud. The right exists where the party is prevented from presenting his cause of action by improper acts that operate upon matters pertaining, not to the judgment itself, but to the manner in which it was procured. *Salvation Army* v. *Morris,* 421 F.2d 805, 807 (10th Cir. 1970).

The grant of the writ of certiorari in this instance would be in the interests of justice and would benefit a large class of taxpayers (perhaps 2,000 past and present Commission employees) for whom the statute of limitations has barred only a portion of their treaty exemption claims. At oral argument in *O'Connor,* government counsel told this Court that the potential recovery in 1986 was in excess of $100 million.

The McKabneys invite the Court's favorable consideration of their petition on the ground that the court of appeals has so far sanctioned a departure from the accepted and usual course of judicial proceedings as to call for the exercise of the Supreme Court's power of supervision.

CONCLUSION

For the foregoing reasons, it is requested that this petition for a writ of certiorari be granted.

Respectfully submitted,

DWIGHT A. MCKABNEY
MERCEDES P. MCKABNEY
P. O. Box 1538
APO Miami, FL 34003
Tel. (011) 507-63-5316
Republic of Panama
Petitioners, Pro Se

September 19, 1988.

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

88-1219

DWIGHT A. MCKABNEY and MERCEDES P. MCKABNEY,
Plaintiffs-Appellants,

MERCER J. TYLER and MIYOJA TYLER,
Plaintiffs,

v.

THE UNITED STATES,
Defendant-Appellee.

DECIDED: June 20, 1988

Before BISSELL, MAYER, AND MICHEL,
Circuit Judges.
PER CURIAM.

DECISION

The order of the United States Claims Court, No. 31-86T (Dec. 3, 1987) dismissing Dwight A. and Mercedes P. McKabney's claim for an income tax refund, is *affirmed.*

OPINION

The McKabneys' claim is foreclosed by the Supreme Court's decision in *O'Connor v. United States,* 107 S. Ct.347

(1986). There, the Court held that while Article XV(2) of the Agreement in Implementation of Article III of the Panama Canal Treaty exempted Commission salaries from taxation by Panama, it did not exempt them from taxation by the United States. The Court said the first section of Article XV "establishes the context for the discussion of tax exemptions in the entire Article - so that when secs. 2 and 3 state that 'United States citizen employees...shall be exempt' from taxes, they are understood to be dealing only with taxes payable in Panama." Id. at 350. Therefore, there is no merit to the argument that the income McKabney earned while working for the Commission should be exempt from United States taxation. *See Scrable v. United States,* 811 F.2d 1202, 1203 (8th Cir. 1987) ("Article XV applies only to Panamanian taxes, and hence petitioners (are) not entitled to refunds of the United States income taxes paid").

The McKabneys contend that the Claims Court should have given them an evidentiary hearing to present "new" evidence showing that *O'Connor* is wrong. But the Supreme Court had much of this allegedly new evidence before it when it decided *O'Connor*; apparently, it found that evidence unpersuasive. In any event, treaty interpretation "'is a question of law and not a matter of fact,'" *Strong v. United States,* 518 F.2d 556, 563 (Ct. Cl. 1975) (quoting *Citizen Band of Potawatomi Indians v. United States,* 391 F.2d 614, 618 (Ct.Cl. 1967)) and, like the Claims Court, we are bound to apply the Supreme Court's unequivocal interpretation of Article XV(2) of the Implementation Agreement. *See, e.g., United States v. Mason,* 412 U.S. 391, 396 (1973).

APPENDIX B

IN THE UNITED STATES CLAIMS COURT

No. 31-86T

Filed: December 3, 1987

DWIGHT A. MCKABNEY, et al.,

Plaintiffs

v.

THE UNITED STATES,

Defendant.

ORDER

Because plaintiffs have not, pursuant to this court's order filed August 5, 1987, shown cause why their claims are different from *Bonnano, et ux. v. United States,* No. 267-84T, the Clerk is directed to dismiss plaintiffs' complaint.

MARIAN BLANK HORN
Acting Chief Judge

APPENDIX C

IN THE UNITED STATES CLAIMS COURT

No. 31-86T

JUDGMENT

Filed Dec 4 1987

DWIGHT A. MCKABNEY, *et al.*,

v.

THE UNITED STATES

Pursuant to the order of December 3, 1987, directing dismissal of the complaint,

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that the complaint is dismissed with costs to the prevailing party.

FRANK T. PEARTREE
Clerk of Court

December 4, 1987

By: Roger L. Neiman
Deputy Clerk

APPENDIX D

IN THE UNITED STATES CLAIMS COURT

No. 267-84T

Filed August 13, 1987

JUSTIN J. and MARGARET M. BONANNO,
Plaintiffs,

v.

THE UNITED STATES,
Defendant.

OPINION

SMITH, Chief Judge

Plaintiffs originally filed suit for a tax refund with this court on October 14, 1986. This court then suspended proceedings on this case pending the ultimate disposition of *Coplin v. United States* and ordered all further adjudications on this claim to be bound by *Coplin's* relevant rulings. *See generally O'Connor v. United States*, 107 S.Ct.347 -U.S.-. (1986) *aff'g, Coplin v. United States,* 761 F.2d 688, *rev'g* 6 Cl.Ct. 115 (1984). With the ultimate decision in Coplin having already been made, the suspension was automatically lifted,

and plaintiffs filed a Motion for Further Proceedings. On the basis of *O'Connor v. United States*, this court is compelled to deny plaintiffs' Motion for Further Proceedings and will accordingly dismiss plaintiffs' complaint.

Facts

Justin J. Bonanno 1/, is a United States citizen who was employed in Panama by the United States Canal Commission (the "Commission"). Plaintiffs' complaint concerns the taxability of Mr. Bonanno's wages earned while he was working for the Commission during the tax years of 1979 through 1985. Although plaintiffs paid taxes on these wages, they later filed a timely claim with the I.R.S. for refund. They contended that his wages derived from the Commission were not taxable as income because of the Panama Canal Treaty, September 7, 1977, United States-Panama, T.I.A.S. No. 10030. Defendant disallowed plaintiffs' claim, and plaintiffs come now before this court requesting relief.

Discussion

I.

Interpretation of Article XV(2) of Article III.

The central focus of plaintiffs' claim is based upon Article XV(2) of Article III of the Panama Canal Treaty, September 7, 1977, United States-Panama, T.I.A.S. No. 10031 (hereinafter Article XV(2)), which

---

1/ Margaret M. Bonanno is named as plaintiff because she signed a joint income tax return with her husband.

states as follows:

> United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees, or other charges on income derived from sources outsideof the Republic of Panama.

Plaintiffs contend that this treaty provision exempts United States citizens from United States and Panamanian taxation on their wages earned at the Panama Canal Commission. Defendant agrees that this treaty provision provides an exemption from Panamanian taxes but contends that it provides no similar exemption from United States taxes.

Although plaintiffs' argument seems plausible from a plain reading of Article XV(2), plaintiffs' argument cannot stand because it runs afoul of the Supreme Court's interpretation of the provision rendered in *O'Connor v. United States. See generally* 107 S.Ct. at 347, -U.S.-. In that case, the Court upheld defendant's present position that Article XV(2) exempts wages of United States citizens employed at the Commission only from Panamanian taxes, not from United States taxes.

Plaintiffs do not dispute the existence of the *O'Connor* holding but instead urge this court to open proceedings anew on the interpretation of Article XV(2) because of some newly-found evidence. This new evidence includes: State Department comments on a draft of Article XV(2); an earlier draft of Article XVI(2) of Article IV; affidavits by Dr. Royo, former

President of the Republic of Panama and second ranking negotiator during the treaty's negotiations; and a statement by Dr. Royo which was previously held by the government and was subsequently declassified by Richard R. Wyrough on May 15, 1986.

Despite this new material, plaintiffs' interpretation still cannot be asserted before this court because of the well-recognized doctrine of stare decisis. This doctrine, which promotes predictability and coherence in the law, *Olson v. Paine,* 806 F.2d 731, 741 (7th Cir. 1986); 20 Am.Jur. 2d sec. 184 (1965), requires a court to follow previous decisions by the same or higher courts even though different parties are involved. 20 Am.Jur. sec. 183. The previous decisions which are binding precedent under stare decisis, of course, do not include findings of fact but only determinations of law. 20 Am.Jur. sec. 190; see *L. E. Myers Co. v. United States,* 10 Cl.Ct. 617, 619 (1986). It is axiomatic that this court cannot disregard the Supreme Court's legal decisions even if it is persuaded that the Supreme Court was in error. *E.g., Jaffree v. Board of School Commissioners,* 459 U.S. 1314, 1315 (1982); *Estate of Bunn v. United States,* 3 Cl.Ct. 547, 549 (1983). But cf. In re Korman, 449 F2d 32, 39 (7th Cir. 1971) (per curiam) (An appellate court can disregard a Supreme Court decision if it is convinced that it has been undermined or repudiated by later decisions of the Court), *rev'd without opinion,* 406 U.S. 952 (1972).

Plaintiffs concede that their interpretation of Article XV(2) cannot stand if stare decisis applies. Plaintiffs instead argue that treaty interpretation is governed by the same principles that apply in domestic

contract law. Therefore, stare decisis would not apply because contract interpretation is a question of fact and not a question of law. A. Corbin, Corbin on Contracts sec. 554, at 522 (1952); E. Farnsworth, Contracts sec. 7.14 at 515 (1982).

It is true that treaty interpretation is similar to contract interpretation in many respects. *See Harris v. United States*, 768 F.2d 1240, 1242 (11th Cir. 1985) ("(I)nternational agreements should be construed more like contracts than statutes."), *vacated and remanded in light of O'Connor v. United States*, 107 S.Ct. 450 (1986); *Board of County Commissioners v. Aerolineas Peruanasa, S.A.*, 307 F.2d 802, 806 (5th Cir. 1962) ("(I)n construing the...(a) treaty as other contracts, we give consideration to the intent of the parties so as to carry out their manifest purpose."), cert. denied, 371 U.S. 961 (1963); *but see Air France v. Saks*, 470 U.S. 392, 397 (1984) ('(T)reaties are construed more liberally than private agreements, and to ascertain their meaning we may look beyond the written words to the history of the treaty, the negotiations, and the practical construction adopted by the parties.' (quoting *Choctaw Nation of Indians v. United States*, 318 U.S. 423, 431-32 (943))). Yet, the analogy cannot be extended to the present situation. Treaty interpretation is not the same as contractual interpretation for treaty interpretation is not a determination of fact. Rather, it is well established that treaty interpretation is considered to be a question of law. *E.g., Strong v. United States*, 207 Ct.Cl. 254, 264, 518 F.2d 556, 563, cert. denied, 423 U.S. 1015 (1975). It must not be forgotten that while treaties have some of the charac

teristics of voluntary agreements between two sovereigns, by our Constitution they have the force of law. *See* U.S. Constitution, Article II, sec. 2, cl. 2. Examination of this treaty's negotiating history and purpose does not render its interpretation a matter of fact but merely serves as an aid to the legal determination which is at the heart of all treaty interpretation. *Cf. Quality Furniture Rentals, Inc. v. United States*, 1 Cl.Ct. 136, 141 (1983) ("(W)here...the language of...(a) statute is nebulous, a clear expression of legislative intent must be given great weight."); *Witco Chem. Corp. v. United States*, 742 F.2d 615, 623 (Fed.Cir. 1984) ("This lack of clarity in the statutory language highlights our need to find that interpretation which...(is) most harmonious with its scheme and...purposes that Congress manifested" (quoting *N.L.R.B. v. Lion Oil Co.*, 352 U.S. 282, 297 (1957))). This Court is, therefore, bound under the doctrine of stare decisis to follow *O'Connor* and to accordingly interpret Article XV(2) as providing United States Commission wages with an exemption only from Panamanian taxation, and not an exemption from United States taxation.

II.

Interpretation of Article XVI(2) of Article IV.

Article XVI (2) of Article IV of the Panama Canal Treaty, September 7, 1977, United States-Panama, T.I.A.S. No. 10032 (hereinafter Article XVI(2)), also fails to provide plaintiffs with an exemption from Uni-

ted States taxation for wages earned at the Commission. 2/ It states, as follows:

> Members of the Armed Forces or the civilian componet, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United States Forces or for any of the service facilities referred to in Articles XI or XVII or this Agreement. Similarly, as is provided by Panamanian law, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

Id. (emphasis added)

The only pertinent difference between this provision and Article XV(2), which was discussed above, is the phrase "as is provided by Panamanian law." The significance of this phrase, however, provides no support on behalf of plaintiffs' position.

The Supreme Court in *O'Connor* may not have directly addressed the scope of the exemption provided in Article XVI(2), but its decision clearly resolved Article XVI(2)'s interpretation by implication. In *O'Connor*, "petitioners contend(ed) that the variation in the phraseology of the two provisions (,Article XV(2) and Article XVI(2),) demonstrate(d) that the taxation provision () of...(Article XV(2) was) meant to be bilateral." *O'Connor v. United States*, 479 U.S.___, 107 S.Ct.

2/ Plaintiffs are not members of the Armed forces or the civilian component, but this provision is considered here to facilitate the interests of judicial economy. Plaintiffs' counsel represents approximately fifty other similar tax refund claims, some of whom are members of the Armed Forces or the civilian component and thus base their claims upon Article XVI(2).

at 352. Yet the Court found that the absence of the phrase, "as is provided by Panamanian law," was of no significance. Thus, if the addition or absence of this phrase provided no significance between the two provisions and Article XV(2) only provides an exemption from Panamanian tax, it can also be inferred that Article XVI(2) only provides an exemption from Panamanian taxes, and not an exemption from United States taxes as well.

Even if this court found the difference in phraseology to be significant, the inclusion of the phrase, "as is provided by Panamanian law," would tend to undercut Plaintiffs' position rather than to support it. This inclusion seems to be a clear indication that the exemption of tax in Article XVI(2) was only for Panamanian taxes. Indeed, it was the absence of this limiting language which the taxpayers raised in *O'Connor* as support for their contention that Article XV(2) exempted both United States and Panamanian taxes. *O'Connor v. United States*, 479 U.S.____, 107 S.Ct. at 352, *aff'g*, 761 F.2d at 688 (limiting language not discussed in appellate opinion), *rev'g, Coplin v. United States*, 6 Cl.Ct. at 137. Specifically, it was taxpayer's argument that the absence of this language raised a negative inference in favor of Article XV(2). Therefore, it is only logical to conclude that the insertion of this language would raise the inference that Article XVI(2) was only intended to exempt United States citizen Commission wages from Panamanian taxes, but not from United States taxes.

Conclusion

Plaintiffs' claim of exemption from United States taxes for wages earned while at the Panama Canal Commission must be rejected. No grounds for relief exist under Article XVI (2) under *O'Connor* because of the doctrine of stare decisis, and no grounds for relief exist under Article XVI under *O'Connor* because of that decision's clear implications. This court will, therefore, deny plaintiffs' Motion for Further Proceedings since to do otherwise at this point would be a wasteful use of judicial resources. If plaintiffs believe that *O'Connor* was incorrectly decided in light of some newly found evidence, they must get the Supreme Court to overrule it. Whatever merits and powers this court may possess, it has not been entrusted by the Framers of our Constitution with appellate review of Supreme Court decisions. *See U.S.* Constitution Article III, sec. 1. Plaintiff's Motion for Further Proceedings is denied, and the Clerk is directed to dismiss plaintiffs' complaint.

IT IS SO ORDERED.

COSTS AWARDED TO THE DEFENDANT.

LOREN A. SMITH
Chief Judge

APPENDIX E

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

88-1219

DWIGHT A. MCKABNEY and
MERCEDES P. MCKABNEY,
Plaintiffs-Appellants,

MERCER J. TYLER and MIYOJA TYLER
Plaintiffs,

v.

THE UNITED STATES,
Defendant-Appellee.

JUDGMENT

ON APPEAL from the United States Claims Court in
CASE NO(S) 31-86T
This CAUSE having been heard and considered, it is
ORDERED and ADJUDGED:

AFFIRMED.
ENTERED BY ORDER OF THE COURT

DATED Jun 20 1988 Francis X. Gindhart. Clerk
Costs: Against, Appellant
Printing ———— $90.44
Total ———— $90.44

ISSUED AS A MANDATE: JUL 11 1988

APPENDIX F

EXCERPT FROM AGREED TEXT OF ARTICLE XVI OF STATUS OF FORCES AGREEMENT (SOFA), AGREEMENT IN IMPLEMENTATION OF ARTICLE IV OF THE PANAMA CANAL TREATY

FEBRUARY 4, 1975

The attached drafts embody the substantive agreements reached between the negotiators of the United States and the Republic of Panama, ad referendum to the Chief Negotiators, on all issues with the exception of Article IX on Telecommunications. It is recognized that further refinements concerning wording and translation may in some instances be required. In that event, representatives of the negotiators of both sides will meet on February 5 to complete those aspects of the negotiation.

Minister S. Morey Bell
Deputy United States Negotiator

Ambassador Nicolas Gonzalez-Revilla
Deputy Panamanian Negotiator

SOFA DRAFT

Dated February 4, 1975

Table of Contents

	Page
Introduction.....	1
Article I - Definitions.....	2
Article II - Non-Intervention Principle.....	5
* * * * * * * * *	
Article XVI - Taxation.....	42
* * * * * * * * *	

February 4, 1975

ARTICLE XVI

TAXATION

(1) The United States Forces, their activities, and the services, facilities, buildings, material, equipment, supplies, and other property acquired, used, or transferred in the Republic of Panama by or on behalf of the United States Forces or their contractors for the purpose of this Agreement shall be exempt from all taxes,

fees, or other charges by the Republic of Panama or any entity or political subdivision thereof. These exemptions shall not extend to the incidence which a net income tax or social security assessment may have on the prices charged by Panamanian suppliers. The Joint Committee will establish implementation procedures for these exemptions.

(2) Members of the forces or the civilian component, and dependents, shall be exempt from taxes, assessments, or other charges to the Republic of Panama or any entity or political subdivision thereof on income received as a result of their services with or employment by the United States Government, on income received from any service facility established and operated under Articles X or XVIII of this Agreement, or on income derived from sources outside of the Republic of Panama. Periods during which such persons are in the Republic of Panama shall not be considered as periods of residence or domicile in the Republic of Panama for the purposes of Panamanian taxation.

APPENDIX G

PARTIAL TRANSCRIPT OF PROCEEDINGS AT FORMAL BOARD MEETING, PANAMA CANAL COMMISSION

JULY 1984

CHAIRMAN GIANELLI: Dr. Cardoze?

DR. CARDOZE: (through the Interpreter) Mr. Chairman, the matter we discuss is so delicate, and it is such a grave matter that I too want to make use of this opportunity to say something because I think we must all make some reference to this matter. I would like to identify myself with the statements of the Vice-President and the Chancellor which represents the feelings of the four Panamanian members of the Board of Directors, and I am sure that this is also the feelings of the entire population of the Republic of Panama.

The matter of the privileges that we discussed and monetary compensation for the loss of those privileges by the U.S. employees of the Commission as of October 1984 is a matter that has a long history behind it. We here in the Panama Canal Commission cannot make an abstraction. The Panama Canal is the expression of the most important factor of the relations between our two countries. I think we will be making a very serious mistake, this Board of Directors -- this Commission will be making a very serious mistake if the COLA is approved as I am sure the administration is recom-

mending with much difficulty.

I personally would be very saddened, and I would feel terrible if this Commission -- if this Board made that decision. I think we would be making a serious mistake and going against the current of our times, and against the special relationship that -- the special relationship between our two countries.

The COLA contradicts what is provided for in the Treaty. The article that refers to the compensation establishes clearly that there will be no discrimination in the matter of salary. It is pointed out that there might continue on with certain -- the employees might continue on with certain privileges, but this is in a limited manner precisely so that these privileges -- the privileges they had as of November 1979 would continue not with the purpose of increasing them.

The whole conception of the Treaty, the whole spirit that governs this relationship, which is a contract of transaction, is to diminish slowly those causes of conflict, those irritants in the relationship in this the most important work that joins our two countries.

I believe that the COLA does not have any justification legally. It is not justified by the Treaty. On the contrary, it goes against the grain of the Treaty itself, against the spirit of the Treaty. On the other hand, to grant such a compensation at the levels that are being expressed--

I want to make a parenthesis here. I didn't want to make any reference to the study made by the consultants because our position to the COLA is much more than the particular aspects of the study, but I am doing this because I read the study. I would probably have

certain questions and certain comments with the consultant, but I didn't want to do that because our position goes beyond the mere study of a COLA.

First there is the matter of the Treaty; then the matter of the austerity policy that we have been living through. We have suffered in the Commission because we know there has been a lessening of the traffic through the Canal, and we know that the administration is making super human (sic) efforts to maintain a balance between revenue and expenses and if after all this, after all this struggle and study and putting our imagination to the budget to see how we could adjust our expenses to meet -- to be in balance with our income, and we have been told that we have to limit certain things, and even capital investments have been affected, and within this administration, Panamanian and U.S. people have been having doubts as to whether the efficiency of the Canal has been affected because of austerity measures.

How is it after all this we are going to tell people we are going to have to make this payment of between five and six million dollars which has not been provided for in the Treaty. So this also contradicts the austerity program.

In the third place, we have debated here, we have argued about the dual salary scale. That has been the object of great discussions between us that has taken up a lot of time, and it has taken up a lot of our discussion for many meetings, even though we know there were other matters that we had to address, and with great rejoicing, and triumph, we were able to eliminate that dual salary scale. We knew what that

meant for the morale of the Panamanian relationship and the relationship between U.S. and Panamanian employees for a more cordial relationship. We managed to do that, and now this very Board of Directors, these very same persons, who barely nine months ago voted, and you voted, you, the U.S. members voted to abolish that dual wage scale, and now whoever is going to vote in favor of this proposal are going to vote to completely go back -- for all practical purposes to go backward.

With all respect, I say this Board would not only be remiss with regard to their duties with regard to the Treaty, but it would be very inconsistent with logic.

Finally, we would also be contradicting something that 's even more transcendental than all of the above, which is the new relationship between our two countries, that special relationship. These Treaties are the product of 70 years of history. When those Treaties established that as of a certain date these privileges must be eliminated, it is because there is a lot of history behind it. It is not because we are against any individual U.S. citizen. Because in this country there is a lot of good feeling toward the United States and their employees, and nobody can accuse Panama of being a country that is anti-American.

But it is something very human in our relationship. Privileges between classes is something that is always hated by all people. It is not tolerated. It is not acceptable. Therefore, I am very concerned that this measure will affect that new relationship, that special relationship between our two countries that are so

closely tied by so many things and that new relationship which is being reflected in this Board, which is the way it should be because we are united by many more things than the things that separate us.

So I do want to repeat that it would be very grave, and we would be making a very serious mistake if we vote in favor of the proposal that the Administrator is making. I repeat, we would be going against what was agreed upon. We would be going against the austerity policy. We would be going against elimination of the dual salary scale and going against that special relationship that we are all interested in fostering, and from every perspective we have been trying to build up. To the U.S. citizens that are here, and are an interested party to this -- we understand that they have an interest in this. We, and here I am talking in the name of all the Panamanian members of the Board, and that is the general feeling in Panama also, we appreciate and we understand the labor, the work that these American citizens are doing for the Panama Canal and we also realize that many of them are very necessary, and their skills are essential for the operation of the Canal. We do appreciate it.

But there are things that are more important than personal interest at a particular point in time. I cannot forget Kennedy's words when he took power in the early years of the '60s when he said to his people, to his U.S. people, do not think what -- do not ask what your country can do for you but what you can do for your country. *I think the U.S. negotiators were wise,* and just as the Panamanian negotiators established that the

privileges would be eliminated -- why did they do that? Because they knew that would be an irritant in the relationship. *Likewise, the American negotiators were very wise. They looked for a manner in which they could give a compensation to the U.S. employees, in fact much more than the COLA could give. There is a clause that says the U.S. citizens will not pay taxes for the salaries that they earn from the Panama Canal Commission.*

So if you believe that it is necessary to grant an additional compensation, then let's not make a mistake. Let us give them -- let's give this additional compensation to all employees, or *if you want to give a special compensation to the U.S. citizens who were here prior to October 1, 1979, and who are going to lose their privileges, then let us look for it in the U.S. Treasury, and probably in the Treaty is already a basis for such a benefit.*

* * * * * * * * *

CHAIRMAN GIANELLI: Other comments?

Well, let me inquire, Minister Ortega. Would the Panamanian members be willing to make some sort of a motion on this subject, following, for example, some of the points made by Mr. Anderson yesterday? Do you have a motion that you would like to put forth before this Board that would reflect your views, your recommendations?

MINISTER ORTEGA: (through the Interpreter) It happens, Mr. Chairman, that in my interventions previously, *Dr. Cardoze had expressed the aspect related to the income tax matter that could be something*

that -- could be an exemption for the U.S. citizen, and that undoubtedly this would be a form of -- it would be a real economic compensation.

I want to add also that if these privileges are agreed upon, nothing will -- the very force that will be benefited by this -- there is nothing that will avoid them from demanding additional COLAs so we will be faced with a problem that will not be resolved in a definite manner. This is a very delicate matter. (Emphasis added.)

APPENDIX H

TRANSLATION OF AFFIDAVIT OF PANAMANIAN TREATY NEGOTIATOR AND EX-PRESIDENT OF PANAMA

OCTOBER 2, 1986

AFFIDAVIT OF DR. ARISTIDES ROYO

I, Aristides Royo, Panamanian citizen, bearer of personal identity card No. 8-102-547, married, of legal age, declare under oath that the following declarations are done according to my true knowledge and understanding with the knowledge that these are done under oath

1. That I was a negotiator of the Torrijos-Carter Treaties, which were signed on September 7, 1977

2. That in my position as negotiator, I participated in the sessions where matters relating to fiscal taxation were discussed

3. That the Panamanian position, many times reiterated, was that United States citizen employees of the Canal pay taxes to the Republic of Panama

4. That the proposal outlined in the preceding paragraph was denied in an emphatic manner by the

North American delegation

5. That confronted with such refusal, I proposed that Panama receive part of the taxes collected by the United States from their subject employees of the Panama Canal

6. That the United States negotiators denied Panama the right to impose taxes on North American citizen employees of the Commission

7. That for Panama it would constitute an offense to her sovereignty that foreign workers not pay taxes to our government and, on the contrary for reasons of nationality, they would pay taxes to another nation not considered now as owner of the interoceanic natural resource nor with the capacity to exercise jurisdiction as it did during the period that the 1903 Treaty was in effect

8. That as a result of the impasse produced, a formula was negotiated which expresses in a concrete manner that

> United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees or other charges on income derived from sources outside the Republic of Panama.

9. As we do not consider the Canal part of the

Government of the United States nor shall it be part of the Panamanian Government until December 31, 1999, and that according to the Treaties, Panama as a sovereign territory granted to the United States the right to manage, operate, and maintain the Canal, it appeared to us that the solution of not paying taxes to neither of the two countries would be the most equitable solution and because of this, it was accepted, submitted to a plebiscite in Panama, and ratified by the Senate of the United States

10. That when the resolution known as paragraph 2 of Article XV was presented by the North American delegation and accepted by the Panamanian delegation, I understood very clearly that it meant that neither of the two countries would assess taxes on the income of the North American citizens for their work with the Panama Canal Commission and because of this the text of the paragraph 2 of Article XV expressed it in explicit form

11. At no time have I been consulted by Minister Fernando Cardoze with whom I have never had any conversation in my life regarding this or any other subject

12. I was called by phone in Madrid when I resided there because of my duties as Ambassador by Mr. Michael Kozak, attorney for the Department of State of the United States, this call being made between January and February, 1985. He questioned me

about the breadth and interpretation of paragraph 2 of Article XV, and I replied that the final version was clear and conclusive and that this version had been approved by both parties, expressing that neither of the two countries would levy taxes on the North American citizens because of their work with the Panama Canal Commission. I also added to Mr. Kozak that it was not under the control of neither the negotiators nor the Panamanian government that the United States could establish taxes in different forms on North American citizens who work abroad, but at the same time reminding him of the text of paragraph 2 of Article XV as it was approved.

/S/
Aristides Royo

AR/mo

I, EFEBO DIAZ HERRERA, Notary Public of the Fourth Circuit of Panama, Cedula Number 9-40-726,

CERTIFY

That the above signature has been recognized as his by the undersigned, and for this reason said signature is authentic

Panama, 2 October 1986

/S/ Witness

/S/ Witness

/S/
EFEBO DIAZ HERRERA
Fourth Notary Public

GENERAL AUTHENTICATION CERTIFICATE

Republic of Panama)
Province of Panama)
City of Panama)
Embassy of the) ss:
United States of)
America)

I certify that the official named below, whose true signature and official seal are, respectively, subscribed and affixed to the annexed document, was, on the 2nd day of October, 1986, empowered to act in the official capacity designated in the annexed document, to which faith and credit are due.

EFEBO DIAZ HERRERA
(Typed Name of Official)

(Signature of Consular Officer)

JAMES F. HUGHES III
(Typed Name of Consular Officer)

Counselor of Embassy for Consular Affairs
and Consul General
(Title of Consular Officer)

October 2, 1986
(Date)

(Seal)

APPENDIX I

IN THE UNITED STATES CLAIMS COURT

NOTICE

JUSTIN J. BONANNO, ET UX.

vs. No. 267-84 T

THE UNITED STATES

Clerk's Office

Washington, D.C., February 3, 1988

To Attorney of Record, Assistant Attorney General and Chief Judge Smith:

Please take notice that in the above case, there has been entered this day on the plaintiff's motion, filed December 23, 1987, to vacate judgment pending appeal

the following order by the Chief Judge:

DENIED without prejudice; the court will entertain appropriate 60(b) motions following the outcome of the appeal in *McKabney et al.* v. *United States,* No. 31-86 T.

Frank T. Peartree, Clerk

(2)

Supreme Court, U.S.
FILED
NOV 22 1988
JOSEPH F. SPANIOL, JR.
CLERK

No. 88-489

In the Supreme Court of the United States

OCTOBER TERM, 1988

DWIGHT A. MCKABNEY AND MERCEDES P. MCKABNEY,
PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

CHARLES FRIED
Solicitor General
Department of Justice
Washington, D.C. 20530
(202) 633-2217

9 pp

TABLE OF CONTENTS

Page

Cases:

Bonanno v. *United States*, 12 Ct. Cl. 769 (1987) 3, 5
Coplin v. *United States*, 761 F.2d 688 (1985) 2, 5
O'Connor v. *United States*, 479 U.S. 27 (1986) 2, 3, 5, 6
Strong v. *United States*, 518 F.2d 556 (Cl. Ct.), cert. denied, 423 U.S. 1015 (1975) 3
Trans World Airlines, Inc. v. *Franklin Mint Corp.*, 466 U.S. 243 (1984) 3
United States ex rel Chunie v. *Ringrose*, 788 F.2d 638 (9th Cir.), cert. denied, 479 U.S. 1009 (1986) 3

Treaties and statutes:

Treaty of Panama Canal, Sept. 7, 1977, art. III, T.I.A.S. No. 10031 1
art. IV 4
art. XV 2, 4
art. XV(2) 1, 2, 3, 4, 5, 6
art. XVI 4
art. XVI(1) 5
art. XVI(2) 4, 5

Tax Reform Act of 1986, Pub. L. No. 99-514, § 1232(a), 100 Stat. 2563-2564 7

In the Supreme Court of the United States

OCTOBER TERM, 1988

No. 88-489

DWIGHT A. MCKABNEY AND MERCEDES P. MCKABNEY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

Petitioners seek review of the decision of the court of appeals (Pet. App. 1a-2a) dismissing their claim that Mr. McKabney's salary from the Panama Canal Commission is exempted from United States taxation under Article XV(2) of the Agreement in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, T.I.A.S. No. 10031.[1]

---

[1] Article XV(2) of the Agreement in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, provides:

> 2. United States citizen employees and dependents shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the Commission. Similarly, they shall be exempt from payment of taxes, fees, or other charges on income derived from sources outside the Republic of Panama.

1. a. In January 1986, petitioners sued in the U.S. Claims Court to recover federal taxes withheld from wages earned by Mr. McKabney from 1979 to 1981 as a civilian employee of the Panama Canal Commission,[2] contending that the pertinent provision of the Panama Canal Treaty Implementation Agreement, Article XV, exempted that income from United States taxation (Pet. 5).

b. Petitioners' suit was suspended pending this Court's review of consolidated cases (Pet. 6 n.2), including the Federal Circuit's decision in *Coplin* v. *United States*, 761 F.2d 688 (1985), that raised the issue of exemption of income earned in Panama from United States taxation. In its decision, *O'Connor* v. *United States*, 479 U.S. 27 (1986), this Court unanimously affirmed the judgment of the Federal Circuit in *Coplin* and ruled that Article XV(2) of the Implementation Agreement was not intended to restrict the right of the United States to tax citizens employed by the Commission.

c. The Claims Court thereafter dismissed petitioners' suit (Pet. App. 3a, 4a), and the Federal Circuit affirmed (*id.* at 1a-2a), holding petitioners' claim foreclosed by this Court's decision in *O'Connor* (*id.* at 1a). The court of appeals rejected petitioners' contention that the Claims Court should have conducted an evidentiary hearing to consider allegedly "new evidence" bearing on the correctness of the *O'Connor* holding. The court stated that "the Supreme Court had much of this allegedly new evidence before it when it decided *O'Connor* [, and] apparently it found that evidence unpersuasive" (*id.* at 2a). In any event, the court observed, "treaty interpretation is a question of law and not a matter of fact" (*ibid.* (citations and

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[2] Mercedes McKabney is a party in this suit because she filed a joint tax return with her husband.

~~and~~ internal quotations omitted)), and the court was bound to apply this Court's "unequivocal" interpretation in *O'Connor* of Article XV(2) of the Implementation Agreement (*ibid.*).

2. Petitioners' challenge was foreclosed by the decision in *O'Connor* v. *United States*, 479 U.S. 27 (1986), and, therefore, was properly dismissed. There is no basis for further review by this Court.

a. In *O'Connor*, this Court held that Article XV(2) of the Implementation Agreement did not exempt salaries earned by American employees of the Panama Canal Commission from United States taxation. The Court examined the plain language of the treaty as well as the actions of both the United States and the Republic of Panama in applying the Treaty's terms. See *O'Connor* v. *United States*, 479 U.S. at 33 (citing *Trans World Airlines, Inc.* v. *Franklin Mint Corp.*, 466 U.S. 243, 259-260 (1984)). The Court determined that the text, consistent with the "overwhelmingly convincing" verbal context of Article XV(2), provided an exemption only from Panamanian taxes (479 U.S. at 31).

Petitioners asked the appeals court to override this Court's interpretation of the Treaty in *O'Connor* on the basis of "new" evidence that, they maintained, warranted a different outcome. The Federal Circuit recognized that, contrary to petitioners' assertion (Pet. 7-9), treaty interpretation is a question of law (*Strong* v. *United States*, 518 F.2d 556, 563 (Cl. Ct.), cert. denied, 423 U.S. 1015 (1975); *United States ex rel Chunie* v. *Ringrose*, 788 F.2d 638, 643 n.2 (9th Cir.), cert. denied, 479 U.S. 1009 (1986)) and that petitioners were, in effect, urging the court to reconsider the legal issue settled by this Court in *O'Connor*. As the Claims Court correctly understood in *Bonanno* v. *United States*, 12 Ct. Cl. 769, 771 (1987), "[i]t is axiomatic that [a lower court] cannot disregard the Supreme Court's legal

decisions even if it is persuaded that the Supreme Court was in error" (Pet. App. 8a (citations omitted)). Accordingly, the appeals court correctly affirmed the dismissal of petitioners' claim.

b. Petitioners argue (Pet. 11-12) that the government's fraudulent conduct throughout the course of the *O'Connor* litigation justified reconsideration of the exemption issue decided in that case. They contend that the government's "nonproduction" of a 1975 draft of Article XVI of the Agreement in Implementation of Article IV of the Panama Canal Treaty[3] was "material" and "inexcusable" (Pet. 13) because the change in language from the 1975 draft to the final version of Article XVI(2) indirectly shows that the final version of Article XV was intended to create an exemption from United States as well as Panamanian taxation (Pet. 14).

Because the 1975 draft of Article XVI had no apparent relevance to the issue in *O'Connor*, which dealt with Article XV—and not Article XVI—of the Agreement, there was no reason for the government to produce it during the *O'Connor-Coplin* litigation. Hence, there was no fraudulent concealment.

Indeed, petitioners' strained suggestion that bilaterality of the exemption in Article XV(2) can be inferred from the evolution of Article XVI(2) rests on a false premise. Their entire argument depends on the erroneous assumption

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[3] The 1975 draft reads as follows (Pet. 12-13):

> (2) Members of the forces or the civilian component, and dependents, shall be exempt from taxes, assessments, or other charges to the Republic of Panama or any entity or political subdivision thereof * * *

Petitioners compare that provision with the final text of Article XVI(2) as it appeared in the treaty agreement in 1977 (Pet. 13):

> (2) Members of the Forces or the Civilian component, and dependents, shall be exempt from any taxes, fees, or other charges on income received as a result of their work for the United States Armed Forces. * * *

that, by replacing the 1975 language in Article XVI(2) that spoke of an exemption "from taxes * * * to the Republic of Panama" with the phrase "any taxes," the drafters expanded the unilateral exemption to a bilateral exemption. However, the final version of Article XVI(2) unquestionably permits United States taxation of armed forces personnel salaries, and creates a unilateral exemption from Panamanian taxation only. Indeed, in the course of arguing that differences in the phraseology of the two articles demonstrated that Article XV(2), unlike Article XVI(2), created a bilateral exemption, the taxpayers in the *O'Connor-Coplin* cases acknowledged that Article XVI(2) does not exempt members of the armed forces from United States taxation. See *O'Connor* v. *United States*, 479 U.S. at 34. The Court rejected petitioners' argument as to Article XV(2), but, in so doing, tacitly accepted their characterization of the final version of Article XVI(2) as creating only a unilateral exemption (*ibid.*).[4]

The Court in *O'Connor* also pointed out that "the structure of Article XV is similar to that of Article XVI," in that the reference in the first section of Article XV to the "*payment in the Republic of Panama* of all taxes," like a similar reference in Article XVI(1) to regulations *of the Republic of Panama*, "establishes the context for the discussion of tax exemptions in the entire article" (479 U.S. at 30 (emphasis added)). Since the reference in the first section of Article XVI "establishes the context" for the second section of that Article, the deletion of the explicit reference to the Republic of Panama from the earlier draft of Article XVI(2) simply eliminated a redundancy.

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[4] The Claims Court in *Coplin* v. *United States*, 6 Cl. Ct. 115, 137 (1984), and in *Bonanno* v. *United States*, 12 Cl. Ct. 769, 773 (1987), also concluded that Article XVI(2) provided no exemption from United States taxation.

In sum, petitioners' claim that the 1975 draft illuminates the meaning of Article XV(2) is meritless, since it depends on the premise that the final version of Article XVI(2) represented a shift from a unilateral to a bilateral exemption—a premise that is entirely unsupported and contravenes the settled interpretation of that provision.

c. Petitioners also contend (Pet. 14) that a "due-process [*sic*] issue arises out of other aspects of the government's conduct" in the *O'Connor-Coplin* litigation. First, petitioners question the authenticity of the Panamanian diplomatic note, delivered to the United States prior to argument in the Federal Circuit in *Coplin*, which stated Panama's position that the relevant articles of the treaty provided an exemption only from Panamanian taxes. Petitioners contend that remarks made in July of 1984 by a member of the Panamanian negotiating board, Dr. Cardoze (Pet. App. 18a), undermine the note's validity, and that the transcript of those remarks was not produced by the government nor introduced in *Coplin*.

This line of argument is entirely without foundation. Both the diplomatic note (see *O'Connor* v. *United States*, 479 U.S. at 33 n.2) and the transcript of the Cardoze remarks (see Brief for Petitioners at 39-42 in *O'Connor* v. *United States, supra*) were part of the record in the *O'Connor* litigation, and neither the Federal Circuit nor this Court found the material helpful to petitioners' position. Thus petitioners do not present "new" evidence that would justify revisiting the question decided in *O'Connor*. In all events, as petitioners acknowledge (Pet. 15), the Court in *O'Connor* found no need to consider the diplomatic note (479 U.S. at 33 n.2), and thus did not rely on it. For this reason, any evidence bearing on its validity provides no occasion to question the Court's controlling decision in that case.

Petitioners also erroneously characterize as "new evidence" (Pet. App. 25a) an affidavit of Dr. Aristides

Rojo that was submitted to the Court, in advance of argument, by the petitioners in the *O'Connor* case (see Gov't C.A. Br. App. C). Although available to this Court, it merited no mention in the *O'Connor* opinion and certainly provides no basis for reconsideration in this case of this Court's holding in *O'Connor*.[5]

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

CHARLES FRIED
Solicitor General

NOVEMBER 1988

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[5] We finally note that the question presented here is not of continuing importance because Section 1232(a) of the Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2563-2564, provides, in relevant part, that for "all taxable years whether beginning before, on, or after the date of the enactment of this Act," no provision of the Panama Canal Treaty or its Implementation Agreements "shall be construed as exempting (in whole or in part) any citizen or resident of the United States from any tax under the Internal Revenue Code of 1954 or 1986." This Court found it unnecessary to address this legislation in *O'Connor*, 479 U.S. at 30 n.1.

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No. 88-489

IN THE

Supreme Court of the United States

October Term, 1987

DWIGHT A. MCKABNEY AND MERCEDES P. MCKABNEY
PETITIONERS,

v.

UNITED STATES OF AMERICA,
RESPONDENT.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

Dwight A. McKabney
Mercedes P. McKabney
P.O. Box 1538
APO Miami, Fl. 34003
Telephone (011) 507-63-5316
Republic of Panama
Petitioners, Pro Se

December 1988

TABLE OF CONTENTS

Cases:	Page
Air France v. Saks, 470 U.S. 392 (1985)	2
Coplin v. United States, 761 F. 2d 688 (Fed. Cir. 1985)	passim
Kolovrat v. Oregon, 366 U.S. 187 (1961)	2
O'Connor v. United States, 479 U.S. 27 (1986)	passim
Santovincenzo v. Egan, 284 U.S. 30 (1931)	2
Sumitomo Shoji America, Inc. v. Avagliano, 457 U.S. 176 (1982)	2
Tucker v. Alexandroff, 183 U.S. 424 (1902)	2
TWA v. Franklin Mint Corp., 466 U.S. 243 (1984)	2
United States v. Reynes, 50 U.S. (9 How.) 127, 147-48 (1850)	2,8
Weaver v. Graham, 450 U.S. 24 (1981)	9

Miscellaneous:	
Agreement in Implementation of Art. III of the Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. 10031, Article XV(2)	passim
Article XVI	6
Agreement in Implementation of Art. IV of the Panama Canal Treaty, Sept. 7, 1977, United States-Panama, T.I.A.S. 10032, Article XVI(2)	passim
Kent, *Commentaries,* vol. 1, p. 174	2
Tax Reform Act of 1986, Pub. L. 99-514, sec. 1232(a), 100 Stat. 2563-64	9

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The Goverment's Memorandum in Opposition raises five arguments that, pursuant to Rule 22.5, are subject to comment in this Reply Brief. Petitioners treat those arguments here, seriatim, in the order in which they appear in the Memorandum.

1. *The finality of original treaty interpretation.* Consistently with its arguments in the courts below, the

Government again states that "treaty interpretation is a question of law." That pronouncement is not limited, however, to the (undisputed) proposition that U.S. treaties are a part of Federal law, as provided by Article II of the Constitution. Instead, the Government's view is that the decision in *O'Connor* v. *United States*, 479 U.S. 27 (1986), fixed the meaning of Article XV(2) (of the Agreement in Implementation of Article III of the Panama Canal Treaty, Sept. 7, 1977, TIAS 10031) permanently, and for all applications.

Such a suggestion is contrary to the long-established rules of treaty interpretation by the judiciary. Treaties are construed by the same course of reasoning that is applied to the interpretation of private contracts. Kent, *Commentaries,* Vol. 1, p. 174;*Tucker* v. *Alexandroff,* 183 U.S. 424 (1902); *Santovincenzo* v. *Egan,* 284 U.S. 30, 40 (1931). The significance of language in international agreements is to be examined in the light of what the parties intended. *Air France* v. *Saks,* 470 U.S. 392 (1985); *TWA* v. *Franklin Mint Corp.,* 466 U.S. 243 (1984). Determining the intent of the parties often will entail a far-ranging inquiry into a variety of materials. *United States* v. *Reynes,* 50 U.S. (9 How.) 127, 147-48 (1850); *Kolovrat* v. *Oregon,* 366 U.S. 187 (1961). "The clear import of treaty language controls unless application of the words...according to their obvious meaning effects a result inconsistent with the intent or expectations of its signatories." *Sumitomo Shoji America, Inc.* v. *Avagliano,* 457 U.S. 176, 180 (1982).

Whatever the source material, the inquiry is factual. Where there is substantial evidence, the trial

court has an obligation to examine it rather than to say that the cause involves an abstract legal question for which there already is an impervious answer. Petitioners urge that the fraud practiced by the Government in this instance led to an interpretation of Article XV(2) that is at odds with both its plain meaning and the intent of the negotiators in 1977.

Attention is invited to the fact that the Government does not cite any decision by this Court for the principle that the meaning of an international agreement lies beyond challenge - even for good cause shown - once it has been pronounced. Neither did the Government produce such authority in the appellate-court proceedings. The McKabneys submit that stare decisis does not preclude a trial to ascertain whether they can develop a substantively different record than that which was before this Court in *O'Connor*.

Inasmuch as the *Coplin-O'Connor* cases were decided on summary judgment, there was no trial on the facts. The claims court's refusal to grant an evidentiary hearing to the present petitioners constituted denial of due process.

2. *Relevance of the evidence withheld.* In its Memorandum, the Government admits for the first time in the course of this case that it withheld the 1975 draft of Article XVI. Heretofore, the respondent's position was that the McKabney claim is under Article XV, not XVI, and -- "in all events, the change in wording of Article XVI(2) is scarcely so pregnant with meaning to warrant further litigation." (Govt. brief in Fed. Cir., p.13). The current admission that the paper was not produced in the discovery proceedings in the prior

lawsuits reads as follows:

> "Because the 1975 draft of Article XVI had no apparent relevance to the issue in *O'Connor*, which dealt with Article XV - and not Article XVI - of the Agreement, there was no reason for the government to produce it during the *O'Connor-Coplin* litigation. Hence, there was no fraudulent concealment." (Mem. at 4).

The significance of the foregoing is twofold. First, by indirection, it confirms petitioners' assertion that the State Department certified by affidavit that all contemporaneous negotiating records pertaining to Article XV had been produced.

Second, the admission in the Memorandum supports petitioners' allegation of extrinsic fraud. This is seen upon reading the language which appears in the Government's brief in *O'Connor* before this Court, as follows:

> "More directly, the language of the provisions in question derives from paragraph 2 of Article XVI of the Agreement in Implementation of Article IV of the Panama Canal Treaty (C.A. App. 88-89), which was modeled after the foregoing provision. That paragraph provides:...."
>
> (Here the final 1977 version of Article XVI(2) was set out.)
>
> (Govt. brief, p. 19, May 1986)

What the Court was not told was that the 1975 version (to which Panama's negotiators had agreed) contained the very language that Justice Scalia would look for, and fail to find, as he wrote -

> "It would be another matter if the variation at

> issue - (he was talking of the difference between Article XV and XVI) - were alteration of the phrase 'Panamanian taxes' in one agreement to merely 'taxes' in the other." (479 U.S._____, 107 S. Ct. at 352).

Under these circumstances, the Government's persistence in claiming that there was no fraudulent concealment of material evidence is disingenuous as well as inexplicable.

3. *The supposed tacit ruling on Article XVI.* The Government, at page 5 of its Memorandum, states imperiously that "the final version of Article XVI(2) unquestionably permits United States taxation of armed forces personnel salaries, and creates a unilateral exemption from Panamanian taxation only." It would seem that Government counsel had overlooked the portion of the Scalia opinion quoted in the preceding paragraph - as well as the Justice's comment as to the lack of evidence that Panama had proposed a bilateral tax exemption (discussed at page 12 of the Petition). Given the dishonest retention of the 1975 draft by the State Department, and the unexplained absence of negotiating records on Article XV in the final weeks of 1977, Justice Scalia was left with grounds only for concluding that Panama had not participated (other than by passive acceptance) in the writing of Articles XV and XVI.

The Government's Memorandum goes on to say that when it ruled against the *O'Connor* taxpayers on their Article XV claims, the Court was *tacitly* holding that Article XVI creates an exemption from only Panamanian taxes. Petitioners note that that issue was not

before the Court, and would refer again to the fact that introduction of the 1975 draft would have filled the gaps in the *Coplin-O'Connor* record that Justice Scalia delineated and found to be adverse to the taxpayers' case.

In the final point under part "2b" of the Memorandum (the para. beginning on p. 5), the argument is hopelessly confused - apparently because of a misunderstanding by Government counsel. The writer quotes from a section of the *O'Connor* opinion where Justice Scalia compares Article XV (Taxation) with Article XVI (Import Duties) - both articles being from the Agreement in Implementation of Article III of the Panama Canal Treaty. These two articles apply to the Panama Canal Commission, its employees and contractors. There was no 1975 draft of either of those articles.

The document withheld by the Government was the 1975 draft of Article XVI (Taxation) which would have been part of the Agreement in Implementation of Article IV of the Panama Canal Treaty. (The text of the 1975 draft appears at pp. 15a through 17a of the Petition.) This latter Agreement applies to the U.S. military forces, their civilian employees and contractors. It is *this* Article XVI, sec. 2, in its 1977 final version, that the Government seeks to show was tacitly construed by the Court in *O'Connor.*

The fact is, however, that Justice Scalia and the Government were writing about different articles designated "XVI" - one on import duties and one on taxation. The result is that the validity of this point in the Government's Memorandum is nil - as is also its conclusion that there is a settled interpretation of *that* (?) *provision.*

4. *The content of the O'Connor record.* The Government argues that the transcript of the Cardoze remarks (Pet. 18a - 24a) was *part of the record* in the Federal Circuit and in this Court. (Mem. 6). Similarly, the Government states that the Royo affidavit (Pet. 25a-29a) was available to this Court. The implication is that those papers were "before the Court", in the ordinary sense of the phrase, and so were available to be treated as evidence of record. Petitioners disagree, for the reasons set out below.

(i) The partial transcript of the July 1984 meeting of the board of directors, Panama Canal Commission, was never produced by the Government. Even though a State Department official was sitting on the Commission's board in July 1984, the Government's brief in the Federal Circuit, filed in November 1984, contained the following statement:

> " Finally, there is nothing in this record that the Republic of Panama ever protested the position taken by the United States in this case. The Department of State, which has reviewed this brief, is unaware of any protest from any official speaking in behalf of that Government." (Govt. brief, Fed. Cir., p. 42)

The appellee-taxpayers in *O'Connor* obtained the transcript and attached it to a motion filed in the court of appeals at the time of oral argument. It was ignored by the deciding panel and it, of course, was not part of the appendix in that court. When the matter reached this Court on writ of certiorari, the parties agreed to present that appellate appendix instead of preparing another. The petitioners in *O'Connor* included the partial tran-

script in their brief on the merits. The Government's Memorandum in the present case refers to that brief but it does not explain how material so presented could become "part of the record."

Under the procedure applicable to diplomatic questions, the Court might have directed the Government to produce the official documents, but it did not do so. Moreover, there is indication in the *O'Connor* opinion that the transcript (as presented) was disregarded or misunderstood. This is seen from the observation by Justice Scalia that Panama, which had four of its own nationals on the Board of the Commission, did not object... to the refusal of the U.S. Government to grant a tax exemption under Article XV(2). The McKabneys submit that the board meeting transcript has not been duly considered at the trial court level (as it would be upon remand of their cause of action) and that the Government falsely reported the status of the matter in its November 1984 brief to the court of appeals.

(ii) The Royo affidavit was lodged with this Court by letter shortly before oral argument in *O'Connor* in March 1986. There was no indication at argument that the affidavit had been considered by the Court - or even accepted under the judicial-notice principle of *United States* v. *Reynes,* 50 U.S. (9 How.) 127, 147-48 (1850). Petitioners here should be given the opportunity to present the Royo evidence by testimony or affidavit in the appropriate lower forum.

5. *The effect of the Tax Reform Act of 1986.* The Government, at page 7 of its Memorandum, concludes in a footnote that, because of a Congressional enactment, "the question presented here is not of continuing impor-

tance." Section 1232(a) of Pub. L. 99-514, Oct. 20, 1986, purports to direct the construction of the Panama Canal Treaty and implementing agreements so as to deny citizens and residents of the United States any tax exemption thereunder.

This Court in *O'Connor* recognized (as the Executive Branch apparently does not) that retroactive application of section 1232(a) would pose constitutional questions, if the exemption were otherwise allowable. *O'Connor,* 479 U.S. at 30, n. 1. Petitioners suggest that this issue is not determinative in the present posture of the case. Upon remand to the trial court, it would become a significant legal issue, but because the law was enacted after oral argument in *O'Connor* there so far has been only perfunctory treatment of it by the parties in the decided cases.

In addition to the cases cited by the Court (which deal with retroactive taxation per se), present petitioners would rely on constitutional prohibitions against legislation that seeks to nullify vested rights. *Weaver* v. *Graham,* 450 U.S. 24, 29 (1981). During the period from treaty effective date on October 1, 1979 until October 20, 1986, petitioners contend that they had rights as third-party beneficiaries under those international agreements, which have not been properly construed due to the fraudulent conduct of the Government.

CONCLUSION

For the foregoing reasons and those stated in the petition, a writ of certiorari should be granted.

Respectfully submitted,

Dwight A. McKabney
Mercedes P. McKabney
P.O. Box 1538
APO Miami, Fl. 34003
Telephone (011) 507-63-5316
Republic of Panama
Petitioners, Pro Se

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